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TESTIMONY BEFORE THE SUBCOMMITTEE ON GENERAL OVERSIGHT AND MINORITY ENTERPRISE, COMMITTEE ON SMALL BUSINESS

(10) James N. Dertouzos



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James N. Dertouzos

Testimony Before the Subcommittee on General Oversight and Minority Enterprise, Committee on Small Business

March 3, 1980

I am going to provide a structural overview of the key media industries and deal primarily with the economic issues related to media concentration and crossownership. This testimony is not based on research conducted by the Rand Corporation and the views and conclusions expressed are my own and should not be interpreted as representing those of Rand or any of the agencies sponsoring its research.

The economic markets that mass media firms participate in are quite complex and interrelated. The appropriate market definition depends crucially on the issue under consideration. Media products are highly differentiated by origin, by transmission technology, by packaging, and by an infinite variety of other attributes which may be relevant to characterization of a particular submarket. Few products are identical, yet most are, for some purposes, substitutes. The important thing to remember is that generalizations about the structure and concentration of the mass media are apt to be inappropriate under certain conditions.

Remaining aware of this limitation of market definitions, I will describe some of the more interesting structural characteristics of firms in industries which can be considered to be part of the mass media. In the process, I hope to raise several public policy issues which are of current importance.

## The Daily Newspaper Industry

Newspaper firms are small businesses. To illustrate, the median circulation for the 1580 daily newspapers publishing in 1977 was 12,000.[1] During that time, typical revenues for a paper of that size were about 1.4 million dollars annually.[2] In addition, there existed about 9000 weekly or semi-weekly newspaper establishments selling an average of 5000 subscriptions. Average revenues were about $100,000 in 1975 with 75 percent of the firms employing fewer than 10 workers.[3]

Although detailed data are not compiled on weekly publications, trends in the daily newspaper industry are well documented.[4] The most dramatic trend, perhaps, involves the demise of direct local competition among firms. That is, only rarely does one find multiple firms located in the same city. Table 1 documents the tendency rather succinctly. By 1978, only 5 percent of all daily newspaper firms were located in cities having more than one paper.

Table 1

COMPETITION IN THE NEWSPAPER INDUSTRY

| Year | No. of Firms in Multi-paper Cities | % of Firms in Multi-paper Cities |
|---|---|---|
| 1923 | 1182 | 60% |
| 1948 | 253 | 17% |
| 1978 | 78 | 5% |

SOURCE: Rosse and Dertouzos (1978)

[1] Rosse and Dertouzos (1978).

[2] Calculated using estimates reported in Rosse (1977).

[3] Sterling and Haight (1978).

[4] See Rosse, Owen, and Dertouzos (1975), or Dertouzos (1976).

A number of explanations have been offered to explain the above phenomenon. However, economics of scale have played a pivotal role in the dominance of one-newspaper towns. It is a fact of newspaper technology that, all things equal, a larger firm is able to produce output (in terms of circulation and/or space) at lower per unit costs than a smaller establishment.

There are three sources of economies of scale. To begin with, expenses incurred in creating and composing content are embedded in the cost of the initial newspaper. Thus, the average cost attributable to "first-copy" expenses falls as circulation rises. Also, reproduction costs decline as the number of copies increases. Finally, there exist economies of scale in the distribution process. Certainly, the distribution costs of one newspaper serving a given number of readers in a particular area are lower per subscriber than are the costs of multiple firms delivering to the same total number of readers.

Thus, economic competition between two similar newspapers seeking to attract the same audience cannot survive in the long run. Eventually one or the other will obtain a size advantage sufficient to allow underpricing in advertising markets. However, if newspapers are able to isolate a population segment and differentiate the newspaper product in order to appeal to that segment, survival may be possible. It is evident that this segmentation is usually defined by market location. Thus, we find numerous firms, each selling a product oriented to the particular city. Of course, if a city's population is large and diverse enough, there is potential for segmentation to occur within a single geographic area. However, the historical record demonstrates that, even in the

largest cities, such segmentation has been quite unstable and unlikely to survive in the long run. This inevitability of newspaper economics has been widely accepted as indicated by passage of the Newspaper Preservation Act, as well as recent Justice Department decisions.

The ownership structure of the daily newspaper industry has also been undergoing rather dramatic changes during the twentieth century. Once dominated by local, family enterprises, newspapers are becoming subsidiaries of larger corporate organizations. Table 2 documents the trend. In 1910, there existed 13 chains owning a total of 62 daily newspapers. Thus, less than 3 percent of all U.S. dailies were associated with groups. By 1930, 55 chains owned 311 dailies which had combined circulations amounting to over 43 percent of total U.S. daily circulation. By 1960, over 30 percent of all dailies were chain-owned. In 1976, nearly 60 percent of all daily newspapers were affiliated with chains. These dailies sold over 70 percent of total U.S. circulation.

This tendency toward group ownership may have resulted in a decline of independent newspaper "voices." Although the degree of newspaper autonomy varies significantly from group to group, a corporation's central management inevitably exerts some influence over the individual enterprises. Thus, one finds that there are fewer than 900 independent daily newspaper voices left in the U.S. today. This represents a 59 percent decline since 1910. The trend is expected to continue in the years ahead.

In 1977, the approximately 167 chains collectively sold over 43 million newspapers daily. Table 3 indicates the nature of the size distribution of newspaper chains for 1977. Knight-Ridder had the

Table 2

CHAIN OWNERSHIP, U.S. DAILY NEWSPAPERS
1910 TO 1976

| Year | Number of Chains | Number[a] of Chain-owned Dailies | Total Number of Dailies | % Chain-owned | % of Daily Circulation of Chain-owned Dailies | Number[b] of Independent Voices |
|---|---|---|---|---|---|---|
| 1910 | 13 | 62 | 2,202 | 2.8% | - | 2,153 |
| 1930 | 55 | 311 | 1,942 | 16.0 | 43.4% | 1,686 |
| 1940 | 60 | 319 | 1,878 | 17.0 | - | 1,619 |
| 1953 | 95 | 485 | 1,785 | 27.0 | 45.3 | 1,395 |
| 1960 | 109 | 560 | 1,763 | 31.8 | 46.1 | 1,312 |
| 1970 | 157 | 879 | 1,748 | 50.3 | 63.0 | 1,026 |
| 1976 | 167 | 1,047 | 1,762 | 59.4 | 71.0 | 882 |

[a] The total reflects dailies, not separate establishments. Thus a single establishment publishing a morning and evening edition is counted as two dailies.

[b] This total reflects the number of different owners = number of chains plus the number of non-chain-owned dailies

Editor and Publisher, July 9, 1977.

Sterling and Haight, (1978).

Table 3

MAJOR NEWSPAPER GROUPS, 1977

| Group | No. of Dailies[a] | U.S. Total | Daily (000) Circulation | U.S. Total |
|---|---|---|---|---|
| Knight-Ridder | 34 | 1.9% | 3,681 | 6.0% |
| Newhouse | 29 | 1.6 | 3,204 | 5.3 |
| Tribune (Chicago) | 6 | .3 | 3,099 | 5.1 |
| Gannett | 73 | 4.1 | 2,772 | 4.5 |
| Scripps-Howard | 17 | 1.0 | 1,895 | 3.1 |
| Times-Mirror | 4 | .2 | 1,880 | 3.1 |
| Dow-Jones[b] | 14 | .8 | 1,783 | 2.9 |
| Hearst | 7 | .4 | 1,436 | 2.4 |
| Cox | 17 | 1.0 | 1,179 | 1.9 |
| New York Times | 10 | .6 | 975 | 1.6 |
| Capital Cities | 4 | .2 | 950 | 1.6 |
| Tompson | 57 | 3.2 | 935 | 1.5 |
| TOTAL 12 GROUPS | 272 | 15% | 23.9 million | 39% |
| 155 OTHER GROUPS | 775 | 44% | 19.7 million | 32% |
| ALL GROUPS | 1,047 | 59% | 43.6 million | 71% |

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[a] Total reflects the number of editions, thus, a firm selling both morning and evening editions is counted as two dailies.

[b] Includes the Wall Street Journal which is not, strictly speaking, a general interest daily.

Editor and Publisher, July 9, 1977.

largest combined circulation of nearly 3.7 million papers daily. Gannett owned 73 dailies at the time of the survey, the most of any newspaper chain. At last count, however, the total had risen to nearly 80. The 12 largest groups own 272 dailies with combined circulation of 24 million, about 40 percent of the U.S. total.

The growth of chains has escalated in recent months and is likely to continue in the future. Of course, the appropriate public policy depends crucially on the underlying economic forces which have encouraged the evolving structure of chain ownership. Unfortunately, the available evidence is extremely sparse and conclusions must remain tentative in the absence of further research.

To begin with, there exists no reliable evidence on the impact of chain ownership on the content creation of newspapers. Of course, it is clear that computer technologies permit the rapid transmission of material from a central office to individual newspapers. Thus, one might suspect that there are significant cost advantages associated with group membership. However, there does exist a well-developed market for news stories (for example, the wire services) and syndicated features. All newspapers have access to a great deal of material created elsewhere. Thus, I suspect that any cost advantages associated with chain membership are insignificant. Of course, this cannot be claimed with certainty and remains an empirical issue.

In addition, newspaper chains do not appear to obtain advantages in input markets. For many inputs (for example, newsprint), firms buy in competitive national markets in which even the largest competitors enjoy no size advantage. Also, preliminary evidence suggests that

large firms and chain members seem to have even less success than do smaller enterprises in dealing with labor unions. Finally, it is not evident that chain-owned newspapers are better equipped to adopt technological change or to acquire capital.[1] Thus, pecuniary economies do not exist and cannot be used to explain or justify the growth of newspaper chains.

Of all the economic forces which have probably promoted the evolving structure of chain ownership, first and foremost might well be the tax laws which encourage the investment of accumulated reserves. Under current IRS regulations, undistributed earnings are not taxed as personal income if used in the acquisition of additional newspaper properties. Small, family-owned enterprises are prime targets of merger activity as a result of the need to expedite estate settlements. The 1978 revisions in the capital gains tax have further encouraged chain growth. Growth achieved via merger or conglomerate activity is treated no differently than internal growth. Surely, if the major incentive for merger involves tax laws quite devoid of any economic rationale, then perhaps government action is justified given the desirability of maintaining a large number of independent and viable media sources.

Media Conglomerates

Due to the inherent complexity and interdependence of the various industries, one cannot examine any medium as if it were totally isolated from forces operating in other related markets. However, the extreme difficulty in precisely characterizing media markets severely hampers

[1] See Dertouzos (1979).

any attempt to approach the issues in a general way. Thus, a formal analysis of the extent and ramifications of media conglomeration is likely to be confronted with numerous hazards. Perhaps this accounts for the pronounced absence of entirely satisfactory research in this area. Yet, we will discover that the same companies are deeply immersed in numerous industries which are organized around the collection and dissemination of ideas and information.

Viewed independently, one finds significant group ownership of both newspapers and television stations. In addition, there are numerous examples of corporate interests in both industries. In fact, holdings often extend into radio broadcasting, magazine distribution, cable T.V. systems, and the movie industry. As a beginning effort to quantify certain elements of this conglomeration, Table 4 summarizes some ownership characteristics of broadcast stations and daily newspapers. Of the 718 television stations in the United States, only 29 percent have no discernable affiliation with any other media establishments. In addition, these stations are likely to be located in smaller markets and have a cumulative audience amounting to about 15 percent of the industry total. Only 40 percent of daily newspapers with 27 percent of U.S. circulation are unaffiliated. For radio stations, 25 percent are owned in combinations greater than two. This grossly understates their strength, however, since the powerful 50,000 watt stations are more typically owned by groups. On average, a conglomerate group owns 7 media establishments. Of course, the distribution is highly skewed with some corporations owning significantly more.

Table 4

GROUP OWNERSHIP OF RADIO AND T.V. STATIONS, AND DAILY NEWSPAPERS, 1977

| | Number of Local Establishments | | | |
|---|---|---|---|---|
| | Total | Newspapers | Radios | T.V. Stations |
| Total Number of Local Establishments | 10,280 | 1,580 | 7,982 | 718 |
| Number of Establishments Owned by Conglomerates* | 3,363 | 948 | 1,971 | 509 |
| Number of Independent Establishments | 6,917 | 632 | 6,011 | 209 |
| % Independent | 67% | 40% | 75% | 29% |
| Share of Audience of Independent Establishments** | | 27% | | 15% |

SOURCE: Rosse and Dertouzos (1978).

*For this summary, a group is defined as owning at least one of the following media combinations: 3 or more radio stations, 2 or more daily newspapers, 2 or more television stations, or any ownership of both a daily newspaper and one broadcast station. There were 439 in all.

**For example, newspapers affiliated with no other media establishment sold 27% of daily circulation in the U.S.

In recent years, attention has been directed to the influence of corporate groups in related media industries. For example, a medium with great future potential, cable (CATV) television, is dominated by owners firmly entrenched in connected markets. Table 5 indicates that 1,179, or 30 percent of all CATV systems, are owned by broadcasting companies. Newspaper interests own 12 percent, and publishers of magazines or books control 13 percent. Despite cable's potential to serve specialized or local interests, only 3 percent are owned by communities or subscribers. Of course, numerous production and distribution complementarities exist between cable and the other industries. Regardless, it is not clear that the aforementioned patterns are in the public interest.

Media conglomerates extend into other related industries. For example, broadcasting and daily newspaper groups also own about 100 general-interest magazines, numerous weekly newspapers, several book publishing facilities, and record companies.

For those concerned about diversity in the "market place" of ideas, the tendency of conglomeration is disturbing. Any reasonable characterization of that market suggests that the various industries cannot be viewed in isolation. Also important from an economic standpoint is the fact that few, if any, important efficiencies of joint ownership or production exist. Incentives for conglomeration within the media are similar to those found generally. Growth and risk spreading are of paramount importance to corporate enterprises. Again, tax benefits and the role of capital markets may be pivotal here. However, the importance of those industries to the functioning of a democratic

Table 5

OWNERSHIP OF CATV SYSTEMS

| Ownership Category | Systems | % of Total |
|---|---|---|
| Broadcaster | 1,179 | 30% |
| Newspaper | 474 | 12 |
| Book or Magazine Publisher | 501 | 13 |
| Program Production Distributor | 772 | 20 |
| Theater | 301 | 8 |
| Telephone | 73 | 2 |
| Community or Subscriber | 106 | 3 |
| Cable or Broadcast Equipment | 422 | 11 |

SOURCE: Television Factbook, 1978, Television Digest, Inc.

society as well as the absence of any strong economic justification for the continued growth of conglomerates suggests a need for investigation of the relevant issues.

## Media Crossownership

The potential dangers of group or conglomerate ownership should be decreased with adequate safeguards imposed by competitive submarkets. The local environment is of primary importance. The question is, how much diversity is available in any individual submarket? The answer may vary depending on which product attribute one wishes to focus on. However, the conclusions with respect to news dissemination, advertising information, or pure entertainment are similar, namely that numerous options, each somewhat differentiated, do exist.

Indeed, the concept of "reasonable interchangeability" played a large role in guiding the FCC in banning new joint ownerships of television stations and newspapers located in the same town. In 1977, 53 newspapers were affiliated with T.V. stations located in the same city. Table 6 shows that just over 3% of chain-owned and independent newspaper firms have such crossownership. However, over 25 percent of the newspaper firms in cities with populations of over 500,000 had affiliations with local television stations. Also, 14 percent of those firms located in cities of between 100 and 500 thousand people were crossowned.

Evidence suggests that newspapers and television stations provide services which compete with one another for consumers as well as advertisers. Studies assessing the impact of crossownership have not been conclusive. No strong evidence has surfaced which supports the

Table 6

NEWSPAPER WITH TV CROSSOWNERSHIP BY CITY-STATE, 1977

| City-Size | Number of Newspaper Firms | Number with TV Crossownership | % |
|---|---|---|---|
| 0-20 | 761 | 1 | 0.1% |
| 20-100 | 622 | 19 | 3.1 |
| 100-500 | 150 | 21 | 14.0 |
| 500+ | 47 | 12 | 25.5 |
| Total | 1,580 | 53 | 3.4% |

SOURCES: Broadcasting Yearbook, 1978.
Editor & Publisher International Yearbook, 1978.

proposition that there are joint economies of local news production. Studies attempting to measure price impacts of crossownership are severely flawed. Thus, continuing research in this area is justified, and the crossownership of television stations and newspapers remains an important issue. Forced divestiture of station holdings involves very sensitive equity considerations, especially since, until 1970, the FCC condoned such combinations and even encouraged them on the grounds that broadcast industries would be further developed as a result, especially in small markets. These considerations should be weighed against the benefits implied by a more competitive environment which safeguards a diverse flow of ideas, information, and entertainment.

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